UZBEKISTAN

TRADE SUMMARY

In 1999, the U.S. trade surplus with Uzbekistan was $313 million, an increase of $200 million from 1998. U.S. merchandise exports to Uzbekistan were $339 million, an increase of $191 million from the level of exports in 1998. Uzbekistan was the United States' 74th largest export market in 1999. U.S. merchandise imports from Uzbekistan were $26 million in 1999, down $8 million from 1998.

Uzbekistan applied for WTO accession in December 1994 but did not initiate substantive discussions until late 1998. Negotiations are currently at an early stage.

IMPORT POLICIES

The government of Uzbekistan restricts imports by means of a system of import contract registration that severely limits the availability of foreign exchange. In 1996, the government of Uzbekistan was well on its way to creating a convertible currency. However, an overvalued official exchange rate and export revenue shortfalls caused by poor harvests that year inspired the government of Uzbekistan instead to tighten the earlier system of foreign exchange quotas. Since then, the government of Uzbekistan has periodically made the system yet more rigorous as foreign currency reserves have continued to dwindle. In 1998 the number of importers given convertibility quotas was cut by one third. The remaining two-thirds saw their quotas slashed in half. Although there was no officially announced policy restricting quotas in 1999, observers estimate that a further one-half of those firms which still had convertibility quotas in 1998 had lost them by the end of 1999. The few firms which retain quotas report that, in practice, they are rarely permitted to convert their soum earnings into hard currency.

Although its primary use is now to lower the overall level of imports and thereby husband scarce foreign exchange, the import contract registration system was designed to enforce Uzbekistan's import substitution development strategy. The government of Uzbekistan uses the system to ensure that scarce foreign currency is used primarily to import capital rather than consumer goods. Annual surveys of foreign companies consistently conclude that currency restrictions are the worst of many serious obstacles to doing business in Uzbekistan.

Foreign companies or foreign joint ventures importing capital goods with their own funds held outside Uzbekistan are also subject *de facto* to the import registration system. Although a 1998 presidential decree exempts such cases from the registration requirement, foreign businesses report that their Uzbek bankers strongly recommend that they register anyway.

Once over this hurdle, imports face the next – the State Customs Committee. Customs clearance is a tedious and capricious bureaucratic process. Even capital equipment imports for U.S.-Uzbek joint ventures are subject to substantial processing delays and often remain in customs for two to three months. In one recent case an American investor waited for three months to process equipment worth $4 million through customs and then was forced to pay $2,500 in customs storage costs. Delays affect all imports as there is no procedure for releasing goods under bond.

Although Uzbekistan's tariff rates have not been extreme by international standards, its excise taxes form an effective barrier to the legal importation of certain goods. The excise tax schedule discriminates against imports of goods subject to the tax. Imported liquor, for example, is subject to an excise tax of 90 percent, whereas the rate for domestically produced spirits ranges from 40 percent to 65 percent. Moreover, the government uses a method of calculating excise taxes specific to imported alcohol and tobacco which results in an actual excise assessment many times higher than the nominal rate.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Uzbekistan continues to use an arbitrary set of technical standards based on outdated Soviet methods. Despite regulations to the contrary, customs officials routinely reject foreign certifications of conformity to these standards. Perishable goods are subject to burdensome phytosanitary tests, making it difficult, for example, for restaurants and hotels to make use of imported foodstuffs. Customs officials often take excess test samples of goods subject to technical standards for their own use.

There are three joint ventures that perform price verifications and otherwise assist in import contract registration. One of these, Intertek Testing Services, is also accredited to perform pre-shipment inspection (PSI) to verify the quality of contracted goods. Only tobacco and alcohol are currently subject to mandatory PSI, but importers may choose to contract PSI for other goods. A December 1997 decree requires the Ministry of Foreign Economic Relations to approve import contract registration of pre-inspected goods within two days. Anecdotal reports from those doing business in Uzbekistan indicate that the decree has succeeded in accelerating the clearance of pre-inspected goods.

GOVERNMENT PROCUREMENT

There is no systematic approach to government procurement in Uzbekistan. Instead, procurement decisions are made in a decentralized and ad hoc manner. Often the procurement practices of the central government are similar to those of many countries, with tenders, bid documents, bids and a formal contract award. However, many tenders are announced with suspiciously short deadlines and are awarded to insider companies. A draft Government Procurement Law produced in mid-1998 by an inter-ministerial working group with support from a USG-provided advisor has not yet been submitted to parliament. The long-term goal of this project is to produce legislation conforming to WTO procurement standards. Uzbekistan is not yet a signatory of the WTO Agreement on Government Procurement.

EXPORT POLICIES

Contrary to WTO standards, the government of Uzbekistan grants some tax benefits, such as tax holidays for Uzbek or foreign joint venture exporters. To conserve foreign exchange, the government has imposed a foreign currency surrender requirement on exporters. Exporters must each surrender 50 percent each quarter (raised recently from 30 percent) of projected earnings of hard currency at the official exchange rate. Since the government and not the firm projects these earnings (on the basis of the previous year's receipts), the surrender quota could amount to more than 50 percent of real earnings if export volume or prices drop. Banks are required to convert all earnings as they come in each quarter until the government-determined quota is met. This feature deprives firms of access to their own supply of hard currency for lengthy periods. Finally, since the official exchange rate is roughly one-fourth of the actual market rate, the conversion requirement means that exporters must increase prices to compensate. This amounts to a tax on exporters and hurts Uzbek competitiveness in world markets.

INTELLECTUAL PROPERTY RIGHTS PROTECTION

The 1994 bilateral trade agreement between the United States and Uzbekistan incorporates provisions on the protection of intellectual property rights (IPR). In 1996 Uzbekistan undertook a comprehensive revision of its copyright law, but significant deficiencies remain in Uzbekistan's protection regime for intellectual property. For example, Uzbekistan does not provide protection for pre-existing works. No protection at all is provided for U.S.

sound recordings, since Uzbekistan is neither a member of the Berne Convention nor a member of the Geneva Phonograms Convention. In addition, Uzbekistan does not provide for civil or criminal *ex parte* search procedures needed for effective anti-piracy enforcement.

With respect to enforcement, Uzbekistan needs to adopt even greater reforms. The fact that the state-owned Uzbek airlines shows pirated U.S. films in flights to the United States and elsewhere is emblematic of the government's disregard for intellectual property rights. On the streets, pirated audio and video tapes and compact disks are sold freely.

SERVICES BARRIERS

The largest barrier to foreign services firms entering the Uzbek market is difficulty in converting the currency. For example, insurance companies must collect their premiums in Uzbek currency and may not pay reinsurance premiums in hard currency on the world market. Likewise claims may only be paid in the unconvertible Uzbek currency. These provisions can only be overcome by a special presidential decree granting the company the right to do business in dollars. To date only a state-owned insurance company, Uzbekinvest, and an American-Uzbek joint venture, Uzaig, have that permission. Although the government of Uzbekistan has created an insurance supervisory board, there is not yet a system of licensing insurance companies. This means that firms can currently only operate in Uzbekistan on the basis of a governmental decree. Uzbek as well as foreign private insurance ventures face these currency and registration difficulties.

A 10 percent withholding tax imposed on reinsurance premiums amounts to a *de facto* disadvantage for U.S. reinsurers vis-a-vis other foreign companies. The tax is not levied on reinsurers in countries that, unlike the United States, have a double taxation treaty with Uzbekistan. U.S. companies would, therefore, have to add the 10 percent charge to their net premiums.

The law grants state-owned companies a monopoly over certain forms of mandatory state insurance (i.e. mandatory insurance paid for out of the state budget). The government of Uzbekistan also determines which companies are permitted to issue each of the 13 types of mandatory non-state insurance, but in some instances, foreign firms are allowed to compete.

Foreign banks may not operate in Uzbekistan except as partners in joint ventures with Uzbek firms. Banking and insurance firms with foreign participation are required to establish a charter capitalization fund of $5 million, whereas the government of Uzbekistan determines the required size of the charter funds of Uzbek firms on a case-by-case basis.

INVESTMENT BARRIERS

Two laws, "On Foreign Investment" and "On Guarantees and Measures Designed to Protect Rights Granted to Foreign Investors" came into effect in April 1998. To be considered "an enterprise with foreign investment" under the new laws, a firm must be at least 30 percent foreign-owned and have initial foreign equity of 150,000 USD. At present there is no legal means for smaller foreign-owned companies to register. Although the laws reduce these capital requirements, they are still high enough to exclude foreign investment by small companies, which have proven to be engines of growth and job creation in other countries. The government of Uzbekistan has postponed consideration of proposals to ease these requirements further. U.S.-owned companies in Uzbekistan face cumbersome registration and licensing requirements. Businesses must register with numerous government organizations and obtain licenses from separate entities. This process is so complex that many Uzbekistani officials themselves have difficulty with it.

Uzbekistan's tax code introduced in 1997 is a great improvement over its predecessor. However, it misses a few important provisions that are part of the business environment in most countries. For example, it allows no credit for VAT on capital goods, including plant, machinery and buildings. This puts firms operating in Uzbekistan at a competitive disadvantage compared to those in countries that do allow such credits. In addition, earnings of foreign-owned enterprises are subject to double taxation; such earnings are taxed once when earned by the enterprise in Uzbekistan and then taxed again when remitted to the foreign parent.

Two tax provisions tend to increase labor costs for foreign firms and to raise salaries higher than those paid by local firms. First, the government of Uzbekistan places a 30 percent "import duty" on the salaries of expatriate staff. Second, Uzbek staff face a 45 percent income tax on salaries as low as 1,200 dollars a year. While most Uzbek companies do not comply with their tax duties, foreign investors generally feel obligated to adhere to the law.

While there are no specific local content laws affecting foreign investors, the tax system differentiates among firms based on the local content of their products.

U.S. companies have complained that Uzbekistani laws are not interpreted or applied in a consistent manner. On many occasions, local officials have interpreted laws in a manner that is detrimental to individual private investors and the business community at large. Companies are particularly concerned with the consistent and fair application of the Foreign Investment Law which contains a number of specific protections for foreign investors.

ANTI-COMPETITIVE PRACTICES

Business people in Uzbekistan note that if they are engaged in a sales or services sector in which either the government of Uzbekistan, or a Uzbek-controlled firm is a competitor, they face more than the usual amount of bureaucratic hurdles and currency conversion problems. A recent example concerns a U.S.-Uzbek joint venture's shipment of pure alcohol to be used in making vodka. The shipment had already been admitted to the country when the government of Uzbekistan issued a new decree requiring special licenses for such imports. Customs officials seized the shipment, by then already awaiting processing, for lacking the import license ex *post facto* and then sold half of the alcohol to the state-owned vodka producer. After over a year of legal wrangling, the company won its case in 1999 in the Supreme Court, but the Customs Committee has requested that the case be reviewed again.

OTHER BARRIERS

American investors unanimously complain that they do not control their corporate bank accounts in Uzbekistan. Every routine banking operation requires official permission. Businesses find that enormous amounts of senior staff time are consumed processing simple transactions. The government of Uzbekistan imposes ceilings on how much money can be withdrawn to pay salaries. All purchases must be made via bank transfers because the government of Uzbekistan uses the banks to do tax accounting. It is not possible to possess a corporate expense account or petty cash. Withdrawing money to pay for airplane tickets, for example, is tedious or impossible. Uzbek companies handle this problem with salary withdrawals for non- existent staff. Western accounting practices prevent American companies from using these deceptive practices.

Currency restrictions, the absence of a modern banking system and the lack of access to computers make electronic commerce virtually impossible in Uzbekistan; bribery and corruption are endemic; and businesses complain that they lack access under Uzbek law to international arbitration. Moreover, the judiciary in Uzbekistan is not independent. In the event of disputes, courts frequently favor firms that are controlled or owned by the state.